

Department of Planning and Budget 2012 Fiscal Impact Statement

1. **Bill Number:** HB777

House of Origin Introduced Substitute Engrossed
Second House In Committee Substitute Enrolled

2. **Patron:** Landes

3. **Committee:** Passed both houses

4. **Title:** Joint Subcommittee to Evaluate Tax Preferences.

5. **Summary:** This bill would establish the Joint Subcommittee to Evaluate Tax Preferences in the legislative branch of government, which would oversee the evaluation of Virginia’s tax preferences. The Joint Subcommittee would have a total membership of fourteen legislative members that would consist of eight members of the House of Delegates and six members of the Senate. The Joint Subcommittee would be permitted to direct that the Department of Taxation, under the Joint Subcommittee’s guidance and instruction, conduct independent evaluations of tax preferences and report its findings to the Joint Subcommittee. The Joint Subcommittee would be authorized to establish a technical advisory group to assist the Joint Subcommittee and the Department of Taxation.

The chairman of the Joint Subcommittee would be required to submit an annual executive summary of the interim activity and work of the Joint Subcommittee by the first day of each regular General Assembly session to the General Assembly and to the Governor.

6. **Budget Amendment Necessary:** See Item 8

7. **Fiscal Impact Estimates:** Final

7a. Expenditure Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Positions</i>	<i>Fund</i>
2012	\$0	0	
2013	\$172,400	2	GF
2014	\$171,400	2	GF
2015	\$171,400	2	GF
2016	\$171,400	2	GF
2017	\$171,400	2	GF
2018	\$171,400	2	GF

The Governor’s introduced budget for the 2012-2014 biennium (House Bill 30) did not include from the general fund to support the creation of this commission. The budget as

originally approved by the House and Senate did not include this funding. The newly introduced House Bill 1301, as passed by the House Appropriations Committee does not include general funds to support this legislation.

- 8. Fiscal Implications:** The establishment of the new Joint Subcommittee result in an annual expenditure impact, estimated to be \$15,400; a general fund budget amendment is necessary. This estimate is based upon 14 legislative subcommittee members (eight members of the House of Delegates and six members of the Senate) meeting approximately four times a year at an average cost of \$75 per member, per meeting for expenses. Expenses would vary depending upon the composition of where the commission members are from.

Consequently, the resulting impact is:

14 members x 4 meetings x \$75 per meeting = \$4,200

Compensation for 14 legislative members = \$200 per day x 14 members x 4 meetings = \$11,200

§4-5.01 C of Chapter 890 the 2011 Virginia Acts of Assembly suspends per diem payments for citizen members.

The Division of Legislative Services may incur costs for legal, research and policy analysis.

Although this bill would require the Division of Legislative Services to provide legal, research, and policy analysis, it also allows the Joint Subcommittee to request the Department of Taxation (Tax) to conduct independent evaluations. To conduct such evaluations, Tax reports that they would need to expand the number and types of preferences that it currently studies. At a minimum, Tax reports they would require funding for two additional full-time professionals to conduct such evaluations, resulting in administrative costs of \$157,000 in FY 2013 and \$156,000 in each subsequent fiscal year. Without additional funding, tax reports they would be able to provide only limited assistance to the Joint Subcommittee. Depending upon the requests of the Joint Subcommittee, Tax reports that they may need additional staff and funding. Tax's staffing level would depend upon the scope and scheduling of the evaluations requested by the Joint Subcommittee.

To avoid a conflict of priorities between the legislative and executive branches of government, the employees responsible for the evaluations required by this study would not be the same employees involved with work conducted for the executive branch.

The existence of the Joint Subcommittee itself would not have a revenue impact. If actions of the Joint Subcommittee result in the repeal or modification of tax preferences, there would likely be a revenue impact.

- 9. Specific Agency or Political Subdivisions Affected:** Department of Taxation, Division of Legislative Services; Division of Legislative Automated Systems, Office of the Clerk of the House of Delegates

10. Technical Amendment Necessary: no

11. Other Comments: Provided below are details provided by Tax regarding prior studies similar in nature.

JLARC Tax Preferences Study

The 2010 General Assembly passed Senate Joint Resolution 21, which required the Joint Legislative Audit and Review Commission (JLARC) to conduct a two-year examination of Virginia individual income tax, corporate income tax, and retail sales and use tax preferences. In its report, JLARC was required to do the following:

- Determine which individual income, corporate income, and sales and use tax preferences are being claimed or taken and to what extent;
- Provide an estimate of the fiscal impact of all such tax preferences claimed or taken;
- Examine the public policies for which the tax preferences were established and whether the desired public policies have been achieved;
- Report on whether other states routinely provide a sunset date for their tax preferences; and
- Establish a proposed mechanism or processes for the ongoing evaluation of the effectiveness of such tax preferences in bringing about the desired public policies for which the tax preferences were established.

JLARC was required to complete its meetings for the first year by November 30, 2010 and for the second year by November 30, 2011. A Commission Draft of the report was published November 14, 2011 and the final report will be submitted to the General Assembly during the 2012 session.

In its report, JLARC provided an overview of Virginia's tax preferences and the overall fiscal impact of these preferences. JLARC then divided existing preferences into various categories and determined the utilization of preferences within each category. The report identified several factors that hinder the effectiveness of certain tax preferences, including the limited use of sunset dates in tax preference bills and the lack of a formal process for evaluating the effectiveness of tax preferences.

The report concluded with the suggestion that the General Assembly establish a joint subcommittee to oversee an ongoing evaluation process. This subcommittee would direct the Department of Taxation to conduct routine evaluations and would assemble a technical advisory group to provide guidance and review findings. JLARC acknowledged in its report that, if such a subcommittee were established, the Department would require additional staff, but the number of additional positions required would depend upon the scope of evaluations established by the joint subcommittee.

Sales and Use Tax Expenditure Study

The 1989 General Assembly passed legislation that required the Department to study all sales and use tax exemptions on a continuous five-year cycle, studying two categories of exemptions each year. The Department was required to publish the Sales and Use Tax Expenditure Study and present it to the Chairmen of the House Finance and Senate Finance Committees in December of each year. The goal of the Sales and Use Tax Expenditure Study was to provide a more complete picture of the revenue impact and policy issues surrounding each of the exemptions contained in the Retail Sales and Use Tax Act. The study included detailed information on the policy, fiscal, and economic impact of the exemptions as well as the apparent rationale for the exemptions and their legislative history. It was believed that the periodic review of sales and use tax exemptions was necessary in order to strengthen oversight and control over the process by which sales tax exemptions are granted. In order to complete the study, the Department needed to employ additional economists and analysts. The Department published its last study in December 1995. The 1996 General Assembly repealed the requirement that the Department conduct the study.

In 2005, the General Assembly reinstated a similar but limited study that required the Department to determine the fiscal, economic, and policy impact of each miscellaneous and nonprofit sales and use tax exemption. Specifically, the Department included the following in its report:

- An estimate of the foregone state and local revenues as a result of each exemption;
- Beneficiaries of each exemption;
- Direct or indirect local, state, or federal government assistance received by the persons or entities granted each exemption, to the extent such information is reasonably available;
- The extent to which a comparable person, entity, property, service, or industry is exempt from the retail sales and use tax in other states, particularly states contiguous to Virginia;
- Any external statutory, constitutional, or judicial mandates supporting an exemption;
- Other Virginia taxes to which the person, entity, property, service, or industry is subject;
- Similar taxpayers who are not entitled to a retail sales and use tax exemption; and
- Other criteria, facts, or circumstances that may be relevant to each exemption.

The Department presented its report to the chairmen of the House and Senate Finance Committees no later than December 1 of each year. Subgroups of the exemptions were reviewed in periodic cycles and reports were issued on a rotating basis. When such reports were completed for each subgroup of the sales and use tax exemptions, the Department was required to repeat the process beginning with the subgroup of exemptions for which a report was made in 2007. No individual exemption was analyzed more frequently than once every five years.

Corporate Tax Preferences Report

In 2005, the General Assembly directed the Department to issue an annual report detailing the amount of income tax relief granted to corporations in the Commonwealth. This report must include the total dollar amount of income tax subtractions, deductions, exclusions, exemptions and credits claimed cumulatively by corporations. Beginning in 2010, this report also includes summary information regarding the types of taxpayers that claim corporate income tax relief, as well as information regarding the number of companies that have qualified for the major business facility job tax credit and the amount of such credits.

The Tax Commissioner is required to issue the corporate tax preferences report annually to the members of the House Appropriations Committee, the House Finance Committee, and the Senate Finance Committee. This report does not reflect all of the exemptions and exclusions available to corporations because not all of them are reported on the Virginia income tax return.

Fiscal Year Tax Credit Report

Beginning in 2011, the Department publishes an annual fiscal year tax credit report as part of its annual report. This report shows the number of individual and corporate taxpayers that claim each tax credit and the dollar amount of tax credits that are claimed each fiscal year.

Proposal

This bill would establish the Joint Subcommittee to Evaluate Tax Preferences in the legislative branch of government, which would oversee the evaluation of Virginia's tax preferences. The Joint Subcommittee would have a total membership of fourteen legislative members that would consist of eight members of the House of Delegates and six members of the Senate. The eight members of the House of Delegates would consist of six members of the House Committee on Finance and two members of the House Committee on Appropriations to be appointed by the Speaker of the House of Delegates, upon the recommendation of the Chairman of the House Committee on Appropriations and the Chairman of the House Committee on Finance, respectively. The six members of the Senate would be appointed by the Senate Committee on Rules, upon the recommendation of the Chairman of the Senate Committee on Finance. The Joint Subcommittee would be responsible for the following:

- Undertaking a systematic review of Virginia's tax preferences;
- Establishing procedures and performance measures to evaluate the effectiveness of tax preferences;
- Recommending a process and guidelines for establishing expiration dates for tax preferences; and
- Submitting an annual report to the General Assembly and the Governor of its recommendations, including which tax preferences should be continued, expanded, modified, or eliminated.

This bill does not specify the extent of the review that would be undertaken annually. Rather, the Joint Subcommittee would have the authority to adopt a schedule for reviewing tax preferences based upon program areas to which the preferences relate.

This bill would require an agency of the executive branch of government to work under a subcommittee of the legislative branch of government. Specifically, the Joint Subcommittee would be permitted to direct that the Department of Taxation, under the Joint Subcommittee's guidance and instruction, conduct independent evaluations of tax preferences and report its findings to the Joint Subcommittee. The Joint Subcommittee would be authorized to establish a technical advisory group to assist the Joint Subcommittee and the Department of Taxation. Such technical advisory group would consist of individuals with tax policy or economic expertise and legislative staff. The Department of Legislative Services would be required to provide legal, research, policy analysis, and other services requested by the Joint Subcommittee. Technical assistance would be provided by the staffs of the House Committee on Appropriations and the Senate Committee on Finance.

The chairman of the Joint Subcommittee would be required to submit an annual executive summary of the interim activity and work of the Joint Subcommittee by the first day of each regular General Assembly session to the General Assembly and to the Governor.

This bill would allow members of the Joint Subcommittee to receive compensation and to be reimbursed for reasonable and necessary expenses as provided in the Appropriations Act, without providing funding for the expenses incurred by the Department.

The effective date of this bill is not specified.

Similar Legislation

House Joint Resolution 85 requires JLARC, with technical assistance from the Department, to study and determine the multiplier effects of various types of income tax credits, public-private partnerships, and other public private investment programs.

House Bill 1233 and Senate Bill 658 require the Tax Commissioner to convene a working group on severance tax issues and to submit a report to the General Assembly by December 1, 2012.

Senate Bill 607 requires the Tax Commissioner to report to the General Assembly once the City of Bristol has notified the Department regarding sales and use tax revenue distribution for qualifying public facilities.

Senate Finance Requirements

The Senate Committee on Finance has been amending tax credit bills to include an enactment clause that requires the Department to submit a report in the year immediately preceding the

sunset date of the tax credit. Such reports would be required to include the following information:

- The number of persons, individuals, or other classes of taxpayers claiming the tax credit in each of the immediately preceding five years;
- The aggregate amount of credits claimed in each of the preceding five years by each class of taxpayers;
- The average amount of credit claimed by each class of taxpayers in each of the preceding five years;
- The average amount of taxes paid, after claiming any credits or deductions, by each class of taxpayers claiming the tax credit in each of the preceding five years;
- Any noted trends in the use of the tax credit; and
- Any other information deemed relevant by the Department.

This reporting requirement has been placed on Senate Bill 131, Senate Bill 578, and House Bill 1183.

In order to produce the reports required under the amended bills, the Department would have to begin accumulating data and conducting surveys soon after the bills become effective. If present staff is diverted to these proposed studies, then the Department would not have the resources to continue performing other critical work. To conduct the proposed studies, the Department would require funding for two additional full-time professionals, resulting in administrative costs of \$157,000 in FY 2013 and \$156,000 in each subsequent fiscal year.

Date: 3/15/12

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